

# INTERNATIONAL STANDARD ON AUDITING (UK) 570 (REVISED)

## GOING CONCERN

(Effective for audits of financial statements for periods commencing on or after 15 December 2019)

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Appendix: Illustrations of Auditor's Reports Relating to Going Concern

International Standard on Auditing (UK) (ISA (UK)) 570 (Revised June 2016), *Going Concern*, should be read in conjunction with ISA (UK) 200 (Revised June 2016), *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (UK)*.

**Interpreting the term "going concern" in this ISA (UK)**

The financial reporting frameworks applicable in the UK generally require the adoption of the **going concern basis of accounting** in financial statements, except in circumstances where management intends to liquidate the entity or to cease trading, or has no realistic alternative to liquidation or cessation of operations. In effect, an entity that does not meet the threshold for that exception is described as a **going concern**. This requirement applies even when there are uncertainties about events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern in the future. Such uncertainties are required to be disclosed in the financial statements when they are material.

The term **going concern assumption** is the defining assumption about the condition of an entity for which adoption of the going concern basis of accounting is appropriate: that the entity is, and will be able to continue as, a going concern. Accordingly, as used in this ISA (UK):

- A. The term "going concern" applies to any entity unless its management intends to liquidate the entity or to cease trading, or has no realistic alternative to liquidation or cessation of operations; and
- B. The term "ability to continue as a going concern" is equivalent to the term "ability to continue to adopt the going concern basis of accounting" in the future.

## Introduction

### Scope of this ISA (UK)

1. This International Standard on Auditing (UK) (ISA (UK)) deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report. (Ref: Para. A1)

### Going Concern Basis of Accounting

2. Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future. General purpose financial statements are prepared on a going concern basis of accounting, unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so. Special purpose financial statements may or may not be prepared in accordance with a financial reporting framework for which the going concern basis of accounting is relevant (e.g., the going concern basis is not relevant for some financial statements prepared on a tax basis in particular jurisdictions). When the use of the going concern basis of accounting is appropriate, assets and liabilities are recorded on the basis that the entity will be able to realize its assets and discharge its liabilities in the normal course of business. (Ref: Para. A2)

### Responsibility for Assessment of the Entity's Ability to Continue as a Going Concern

3. Some financial reporting frameworks contain an explicit requirement for management<sup>1a</sup> to make a specific assessment of the entity's ability to continue as a going concern, and standards regarding matters to be considered and disclosures to be made in connection with going concern. For example, International Accounting Standard (IAS) 1 requires management to make an assessment of an entity's ability to continue as a going concern.<sup>1</sup> The detailed requirements regarding management's responsibility to assess the entity's ability to continue as a going concern and related financial statement disclosures may also be set out in law or regulation.
4. In other financial reporting frameworks, there may be no explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern. Nevertheless, where the going concern basis of accounting is a fundamental principle in the preparation of financial statements as discussed in paragraph 2, the preparation of the financial statements requires management to assess the entity's ability to continue as a going concern even if the financial reporting framework does not include an explicit requirement to do so.
5. Management's assessment of the entity's ability to continue as a going concern involves making a judgment, at a particular point in time, about inherently uncertain future outcomes of events or conditions. The following factors are relevant to that judgment:
  - The degree of uncertainty associated with the outcome of an event or condition increases significantly the further into the future an event or condition or the

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<sup>1a</sup> In the UK, those charged with governance are responsible for the preparation of the financial statements and the assessment of the entity's ability to continue as a going concern.

<sup>1</sup> IAS 1, *Presentation of Financial Statements*, paragraphs 25–26.

outcome occurs. For that reason, most financial reporting frameworks that require an explicit management assessment specify the **minimum** period for which management is required to take into account all available information.

- The size and complexity of the entity, **including** the nature and condition of its business and the degree to which it is affected by external factors affect the judgment regarding the outcome of events or conditions.
- Any judgment about the future is based on information available at the time at which the judgment is made. Subsequent events may result in outcomes that are inconsistent with judgments that were reasonable at the time they were made.

### *Responsibilities of the Auditor*

6. The auditor's responsibilities are to obtain sufficient appropriate audit evidence regarding, and conclude on:

- Whether a material uncertainty related to going concern exists; and
- The appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements.

These responsibilities exist even if the financial reporting framework used in the preparation of the financial statements does not include an explicit requirement for management to make a specific assessment of the entity's ability to continue as a going concern.

7. However, as described in ISA (UK) 200 (Revised June 2016),<sup>2</sup> the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for future events or conditions that may cause an entity to cease to continue as a going concern. The auditor cannot predict **with certainty** such future events or conditions. Accordingly, the absence of any reference to a **material uncertainty related to going concern** in an auditor's report cannot be viewed as a guarantee as to the entity's ability to continue as a going concern.

### **Effective Date**

8. This ISA (UK) is effective for audits of financial statements for periods **commencing on or after 15 December 2019**. Earlier adoption is permitted.

### **Objectives**

9. The objectives of the auditor are:

- (a) To obtain sufficient appropriate audit evidence regarding, and conclude on:
  - (i) Whether a material uncertainty related to going concern exists; and
  - (ii) The appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements; and
- (b) To report in accordance with this ISA (UK).

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<sup>2</sup> ISA (UK) 200 (Revised June 2016), *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (UK)*, paragraphs A53–A54.

## Definitions

9-1. For purposes of the ISAs (UK), the following terms have the meanings attributed below:

- (a) Management bias – A lack of neutrality by management in the preparation of information;
- (b) Material uncertainty related to going concern – An uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern, where the magnitude of its potential impact and likelihood of occurrence is such that appropriate disclosure of the nature and implications of the uncertainty is necessary for:
  - (i) In the case of a fair presentation financial reporting framework, the fair presentation of the financial statements; or
  - (ii) In the case of a compliance framework, the financial statements not to be misleading. (Ref: Para. A2-1–A2-2)

## Requirements

### Risk Assessment Procedures and Related Activities

10-1. When obtaining an understanding of the entity and its environment, the applicable financial reporting framework and the entity's internal control as required by ISA (UK) 315 (Revised June 2016),<sup>3</sup> the auditor shall design and perform risk assessment procedures to obtain audit evidence that provides an appropriate basis for the identification of: (Ref: Para. A3–A5)

- (a) Events or conditions that may cast significant doubt on the entity's ability to continue as a going concern; and (Ref: Para. A3–A3-1)
- (b) Whether or not a material uncertainty related to going concern exists.

10-2. In performing risk assessment procedures, the auditor shall obtain an understanding of the following matters:

#### *The Entity and Its Environment*

- (a) The entity's business model, objectives, strategies and related business risks; (Ref: Para. A3-2–A3-3)
- (b) The nature of the entity, including its operations, the types of investments or disposals the entity is making and plans to make, and how the entity is structured and financed; (Ref: Para. A3-4)
- (c) The measurement and review of the entity's financial performance, including forecasts, future cash flows, and management's budgeting processes; (Ref: Para. A3-5–A3-8)

#### *Applicable Financial Reporting Framework*

- (d) The requirements of the applicable financial reporting framework relating to going concern, and the related disclosures that the auditor expects to be included in

<sup>3</sup> ISA (UK) 315 (Revised June 2016), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 5.

the entity's financial statements; (Ref: Para. A3-9)

*The Entity's System of Internal Control*

- (e) The nature and extent of oversight and governance that the entity has in place over management's assessment of the entity's ability to continue as a going concern; (Ref: Para. A3-10–A3-12)
  - (f) How the entity's risk assessment process:
    - (i) Identifies business risks relating to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern;
    - (ii) Assesses the significance of those risks, including the likelihood of their occurrence and their potential impact; and
    - (iii) Addresses those risks;
  - (g) The results of the entity's process as described in paragraph 10-2(f);
  - (h) The entity's information system, and related business processes, as it relates to going concern, including:
    - (i) How the information system identifies and captures events or conditions that may cast significant doubt on the entity's ability to continue as a going concern;
    - (ii) How management identifies the relevant method, assumptions and data that are appropriate in assessing the entity's ability to continue as a going concern; (Ref: Para. A3-13–A3-15)
    - (iii) How the financial reporting process used to prepare the entity's financial statements captures disclosures related to the entity's ability to continue as a going concern.
- 10-3. Where management has not yet performed an assessment of the entity's ability to continue as a going concern, the auditor shall request management to make its assessment.
- 10-4. The auditor shall inquire of management as to its knowledge of events or conditions beyond the period of management's assessment that may cast significant doubt on the entity's ability to continue as a going concern. If such events or conditions are identified, the auditor shall request management to evaluate the potential significance of the event or condition on its assessment of the entity's ability to continue as a going concern. (Ref: Para. A6-1–A6-2)
- 10-5. The auditor shall evaluate whether events or conditions that may cast significant doubt on the entity's ability to continue as a going concern give rise to a risk of management bias in the preparation of the financial statements.
11. The auditor shall remain alert throughout the audit for audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. (Ref: Para. A6-3–A7-1)

*Identification of Previously Unidentified or Undisclosed Events or Conditions* (Ref: Para. A7-2–A7-3)

- 11-1. If the auditor identifies events or conditions that may cast significant doubt on the entity's ability to continue as a going concern, that management has not previously identified or disclosed to the auditor, the auditor shall:
- (a) Request management to perform additional procedures to understand the effect of the events or conditions on management's going concern assessment;
  - (b) Inquire as to why management's going concern assessment failed to identify or disclose the events or conditions; and
  - (c) Perform additional audit procedures relating to the newly identified events or conditions in accordance with paragraphs 12-1–12-2.

**Evaluating Management's Assessment**

- 12-1. The auditor shall perform audit procedures, that include procedures designed and performed in accordance with paragraphs 12-2–13, to obtain sufficient appropriate audit evidence about:
- (a) Whether events or conditions exist that may cast significant doubt on the entity's ability to continue as a going concern;
  - (b) Whether or not a material uncertainty related to going concern exists; and
  - (c) The appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements.
- 12-2. The auditor shall perform audit procedures that include: (Ref: Para. A8–A10-1, A11-1–A12)
- (a) Evaluating management's method to assess the entity's ability to continue as a going concern, including determining if:
    - (i) The method selected is appropriate in the context of the applicable financial reporting framework and the auditor's understanding of the entity; (Ref: Para. A8-3)
    - (ii) Changes from the method used in prior periods are appropriate; and
    - (iii) Whether the calculations are applied in accordance with the method and are mathematically accurate.
  - (b) Evaluating the relevance and reliability of the underlying data used to make the assessment; (Ref: Para. A8-4–A8-5)
  - (c) Evaluating the assumptions on which management's assessment is based by determining whether there is adequate support for the assumptions underlying management's assessment. This shall include determining: (Ref: Para. A8-6–A8-8)
    - (i) Whether the assumptions are appropriate in the context of the applicable financial reporting framework, and if applicable, changes from prior periods are appropriate; and

- (ii) Whether the assumptions are consistent with each other and with related assumptions used in other areas of the entity's business activities, based on the auditor's knowledge obtained in the audit.
- (d) Evaluating management's plans for future actions in relation to its going concern assessment, including determining whether the outcome of these plans is likely to improve the situation and whether management's plans are feasible in the circumstances. (Ref: Para. A8-9–A8-14)
- (e) Considering whether any additional facts or information have become available since the date on which management made its assessment.
- (f) Requesting written representations from management and, where appropriate, those charged with governance, regarding their plans for future actions and the feasibility of these plans. (Ref: Para A8-15)

12D-3. In accordance with ISA (UK) 200 (Revised June 2016),<sup>3a</sup> the auditor shall maintain professional skepticism throughout the audit and in particular when reviewing future cash flow relevant to the entity's ability to continue as a going concern. (Ref: Para. A10-1)

13-1. When performing audit procedures in accordance with paragraph 12-1–12-2, the auditor shall:

- (a) Cover the same period as that used by management to make its assessment of the entity's ability to continue as a going concern as required by the applicable financial reporting framework, or by law or regulation if it specifies a longer period; and
- (b) Consider whether management's assessment includes all relevant information, including all available information about the future, of which the auditor is aware as a result of the audit. (Ref: Para. A11–A11-3)

14-1. If management's assessment of the entity's ability to continue as a going concern covers less than twelve months from the date of approval of the financial statements as defined in ISA (UK) 560,<sup>4</sup> the auditor shall request management to extend its assessment period to at least twelve months from that date.<sup>4a</sup>

#### Management Unwilling to Make or Extend Its Assessment

15-1. If management is unwilling to make or extend its assessment when requested to do so by the auditor, the auditor shall discuss the matter with management, and if appropriate, with those charged with governance. If management, or those charged with governance, do not provide sufficient information about the entity's ability to continue as a going concern, the auditor shall: (Ref: Para. A13-1)

- (a) Consider the implications for the audit in accordance with paragraph 17-2; and

<sup>3a</sup> ISA (UK) 200 (Revised June 2016), paragraph 15.

<sup>4</sup> ISA (UK) 560, *Subsequent Events*, paragraph 5(b).

<sup>4a</sup> In the UK, the period used by those charged with governance in making their assessment is usually at least one year from the date of approval of the financial statements.



- (b) Determine whether there is a significant deficiency in internal control with regard to management's assessment of the entity's ability to continue as a going concern.

### **UK Corporate Governance Code Reporting – Statement on the Directors' Assessment of the Ongoing Viability of the Entity**

16-1. For entities that are required,<sup>4b</sup> and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, or to explain why they have not, the auditor shall perform such procedures as are necessary in the auditor's professional judgment to identify whether there is a material inconsistency between the auditor's knowledge obtained in the audit, including that obtained in the evaluation of management's assessment of the entity's ability to continue as a going concern in accordance with paragraphs 12-1–15-1, and: (Ref: Para. A16-1–A16-2)

- (a) The Board's confirmation in the annual report that it has carried out a robust assessment of the entity's emerging and principal risks;
- (b) The disclosures in the annual report that describe those principal risks, what procedures are in place to identify emerging risks and an explanation of how these are being managed or mitigated;
- (c) The Board's statement in the financial statements about whether it considered it appropriate to adopt the going concern basis of accounting in preparing them, and its identification of any material uncertainties to the entity's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements;
- (d) The Board's explanation in the annual report as to how it has assessed the prospects of the entity, over what period it has done so and why it considers that period to be appropriate; and
- (e) The Board's statement as to whether it has a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of its assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

### **Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained**

17-1. Based on the audit procedures performed and the audit evidence obtained, the auditor shall evaluate whether sufficient appropriate audit evidence has been obtained regarding, and shall conclude on:

- (a) Whether, in the auditor's judgment, a material uncertainty related to going concern exists; and (Ref: Para. A17-1)
- (b) The appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements.

17-2. If the auditor has not obtained sufficient appropriate audit evidence, the auditor shall attempt to obtain further audit evidence. If the auditor is unable to obtain further audit evidence, the auditor shall consider the implications for the auditor's opinion on the

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<sup>4b</sup> In the UK, these include companies with a premium listing of equity shares regardless of whether they are incorporated in the UK or elsewhere.

financial statements in accordance with ISA (UK) 705 (Revised June 2016).  
(Ref: Para. A18-1)

- 18-1. In making the evaluation and conclusions required by paragraph 17-1, the auditor shall:
- (a) Evaluate whether judgments and decisions made by management in making its assessment, even if they are individually reasonable, are indicators of possible management bias. When indicators of possible management bias are identified, the auditor shall evaluate the implications for the audit; and (Ref: Para. A19-1–A19-3)
  - (b) Take into account all relevant audit evidence obtained, whether corroborative or contradictory.

### **Disclosures Related to Going Concern**

#### *Appropriateness of Disclosures When Events or Conditions Have Been Identified and a Material Uncertainty Related to Going Concern Exists*

19. If the auditor concludes that management's use of the going concern basis of accounting is appropriate in the circumstances but a material uncertainty related to going concern exists, the auditor shall determine whether the financial statements: (Ref: Para. A23)
- (a) Appropriately disclose the principal events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and management's plans to deal with these events or conditions; and
  - (b) Disclose clearly that there is a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.

#### *Appropriateness of Disclosures When Events or Conditions Have Been Identified but No Material Uncertainty Related to Going Concern Exists*

20. If events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern but, based on the audit evidence obtained the auditor concludes that no material uncertainty related to going concern exists, the auditor shall evaluate whether, in view of the requirements of the applicable financial reporting framework, the financial statements provide appropriate disclosures about these events or conditions. (Ref: Para. A24–A25)

### **Implications for the Auditor's Report**

#### *Use of Going Concern Basis of Accounting Is Inappropriate*

21. If the financial statements have been prepared using the going concern basis of accounting but, in the auditor's judgment, management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, the auditor shall express an adverse opinion. (Ref: Para. A26–A27)

*Use of Going Concern Basis of Accounting is Appropriate*

- 21-1. If the auditor concludes that the going concern basis of accounting is appropriate, the auditor shall include a section in the auditor's report with the heading "Conclusions relating to Going Concern" and include: (Ref: Para. A27-1–A27-3)
- (a) An explanation of how the auditor evaluated management's assessment of the entity's ability to continue as a going concern and, where relevant, key observations arising with respect to that evaluation;
  - (b) Where the auditor concludes that no material uncertainty related to going concern has been identified, a statement that the auditor has not identified a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorized for issue;
  - (c) A conclusion that management's use of the going concern basis of accounting in the preparation of the entity's financial statements is appropriate; and
  - (d) For entities that are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, or to explain why they have not, the auditor has nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements.

*Use of Going Concern Basis of Accounting Is Appropriate but a Material Uncertainty Related to Going Concern Exists*

*Appropriate Disclosure of a Material Uncertainty Related to Going Concern Is Made in the Financial Statements*

22. If appropriate disclosure about the material uncertainty related to going concern is made in the financial statements, the auditor shall express an unmodified opinion and the auditor's report shall include a separate section under the heading "Material Uncertainty Related to Going Concern" to: (Ref: Para. A28–A31)
- (a) Draw attention to the note in the financial statements that discloses the matters set out in paragraph 19;
  - (b) State that these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the auditor's opinion is not modified in respect of the matter; and
  - (c) For entities that are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, or to explain why they have not, a statement that the auditor has nothing material to add or draw attention to in respect of the directors' identification in the financial statements of any material uncertainties to the entity's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements.

**Appropriate Disclosure of a Material Uncertainty Related to Going Concern Is Not Made in the Financial Statements**

23. If appropriate disclosure about the material uncertainty related to going concern is not made in the financial statements, the auditor shall: (Ref: Para. A32–A33)
- (a) Express a qualified opinion or adverse opinion, as appropriate, in accordance with ISA (UK) 705 (Revised June 2016)<sup>5</sup>; and
  - (b) In the Basis for Qualified (Adverse) Opinion section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not appropriately disclose this matter.

**UK Corporate Governance Code Reporting – Statement on the Directors' Assessment of the Ongoing Viability of the Entity**

- 24-1. For entities that are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, or to explain why they have not, the auditor shall determine whether the auditor has anything material to add or to draw attention to in the auditor's report in relation to paragraphs 16-1(a)–(e), and shall report in accordance with the requirements of paragraph 21-2 and ISA (UK) 720 (Revised June 2016).<sup>5a</sup>
- 24-2. Matters the auditor considers when determining whether there is anything to add or to draw attention to in the auditor's report on the financial statements in accordance with paragraph 24-1 shall include, based on the auditor's knowledge obtained in the audit, including that obtained in the evaluation of management's assessment of the entity's ability to continue as a going concern:
- (a) Whether the auditor is aware of information that would indicate that the annual report and accounts taken as a whole is not fair, balanced and understandable in relation to the entity's emerging and principal risks; and
  - (b) Matters relating to the robustness of the directors' assessment of the entity's emerging and principal risks and its outcome, including the related disclosures in the annual report and accounts, that the auditor communicated to the audit committee<sup>5b</sup> and that are not appropriately addressed in the section of the annual report that describes the work of the audit committee.

**Communication with Those Charged with Governance**

25. Unless all those charged with governance are involved in managing the entity,<sup>6</sup> the auditor shall communicate with those charged with governance events or conditions identified that may cast significant doubt on the entity's ability to continue as a going

<sup>5</sup> ISA (UK) 705 (Revised June 2016), *Modifications to the Opinion in the Independent Auditor's Report*.

<sup>5a</sup> ISA (UK) 720 (Revised June 2016), *The Auditor's Responsibilities Relating to Other Information*, paragraph 22-4.

<sup>5b</sup> ISA (UK) 260 (Revised June 2016), *Communication with Those Charged with Governance*, paragraph 16-1(e).

<sup>6</sup> ISA (UK) 260 (Revised June 2016), paragraph 13.

concern. Such communication with those charged with governance shall include the following: (Ref: Para. A34-1)

- (a) Whether the events or conditions constitute a material uncertainty related to going concern;
- (b) Whether management's use of the going concern basis of accounting is appropriate in the preparation of the financial statements;
- (c) The appropriateness of related disclosures in the financial statements; and
- (d) Where applicable, the implications for the auditor's report.

### **Communication with Regulatory and Enforcement Authorities**

25-1. When the auditor considers that it may be necessary to include a "Material Uncertainty Related to Going Concern" paragraph in the auditor's report<sup>6a</sup> or issue a qualified, adverse or disclaimer of opinion in respect of matters related to going concern,<sup>6b</sup> the auditor shall determine whether law, regulation or relevant ethical requirements: (Ref: Para. A35-1–A35-4)

- (a) Require the auditor to report to an appropriate authority outside the entity;
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

### **Significant Delay in the Approval of Financial Statements**

26. If there is significant delay in the approval of the financial statements by management or those charged with governance after the date of the financial statements, the auditor shall inquire as to the reasons for the delay. If the auditor believes that the delay could be related to events or conditions relating to the going concern assessment, the auditor shall perform those additional audit procedures necessary, as described in paragraphs 12-1–12-2, as well as consider the effect on the auditor's conclusion regarding the existence of a material uncertainty related to going concern, as described in paragraph 17-1(a).

### **Documentation**

26-1. The auditor shall include in the audit documentation:

- (a) Key elements of the auditor's understanding of the entity and its environment, including the entity's internal control related to going concern;
- (b) Indicators of possible management bias related to going concern, if any, and the auditor's evaluation of the implications for the audit.
- (c) Significant judgments relating to the auditor's determination of:
  - (i) Whether or not a material uncertainty related to going concern exists;
  - (ii) The appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements; and
  - (iii) The appropriateness of management's disclosures in the financial

<sup>6a</sup> See paragraph 22 of this ISA (UK).

<sup>6b</sup> See paragraphs 21, 23 and A33 of this ISA (UK).

statements.

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## Application and Other Explanatory Material

### Scope of this ISA (UK) (Ref: Para 1)

- A1. ISA (UK) 701<sup>7</sup> deals with the auditor's responsibility to communicate key audit matters in the auditor's report. That ISA (UK) acknowledges that, when ISA (UK) 701 applies, matters relating to going concern may be determined to be key audit matters, and explains that a material uncertainty related to going concern is, by its nature, a key audit matter.<sup>8</sup>

### Going Concern Basis of Accounting (Ref: Para. 2)

#### *Considerations Specific to Public Sector Entities*

- A2. Management's use of the going concern basis of accounting is also relevant to public sector entities. For example, International Public Sector Accounting Standard (IPSAS) 1 addresses the issue of the ability of public sector entities to continue as going concerns.<sup>9</sup> Going concern risks may arise, but are not limited to, situations where public sector entities operate on a for-profit basis, where government support may be reduced or withdrawn, or in the case of privatization. Events or conditions that may cast significant doubt on an entity's ability to continue as a going concern in the public sector may include situations where the public sector entity lacks funding for its continued existence or when policy decisions are made that affect the services provided by the public sector entity.

### Definitions

#### *Material Uncertainty Related to Going Concern (Ref: Para. 9-1)*

- A2-1. Some financial reporting frameworks may explicitly acknowledge the concept of a material uncertainty, such as IAS 1, but may use different terms when discussing the uncertainties related to events or conditions which may cast significant doubt on the entity's ability to continue as a going concern that are required to be disclosed in the financial statements (e.g., significant uncertainty).
- A2-2. Financial reporting frameworks may not define a material uncertainty. However, for the purpose of this ISA (UK), determining whether a material uncertainty related to going concern exists involves management's assessment of:
- (a) the likelihood of events or conditions occurring; and
  - (b) their potential impact.

Uncertainties relating to such events or conditions are considered material if their disclosure could reasonably be expected to affect the economic decisions of users of the financial statements.

<sup>7</sup> ISA (UK) 701, *Communicating Key Audit Matters in the Independent Auditor's Report*.

<sup>8</sup> See paragraphs 15 and A41 of ISA (UK) 701.

<sup>9</sup> IPSAS 1, *Presentation of Financial Statements*, paragraphs 38–41.

## **Risk Assessment Procedures and Related Activities**

### *Events or Conditions That May Cast Significant Doubt on the Entity's Ability to Continue as a Going Concern* (Ref: Para. 10-1)

A3. The following are examples of events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. This listing is not all-inclusive nor does the existence of one or more of the items always signify that a material uncertainty related to going concern exists.

#### Financial

- Net liability or net current liability position.
- Fixed-term borrowings approaching maturity without realistic prospects of renewal or repayment; or excessive reliance on short-term borrowings to finance long-term assets.
- Indications of withdrawal of financial support by creditors.
- Negative operating cash flows indicated by historical or prospective financial statements.
- Adverse key financial ratios.
- Substantial operating losses or significant deterioration in the value of assets used to generate cash flows.
- Arrears or discontinuance of dividends.
- Inability to pay creditors on due dates.
- Inability to comply with the terms of loan agreements.
- Change from credit to cash-on-delivery transactions with suppliers.
- Inability to obtain financing for essential new product development or other essential investments.

#### Operating

- Management intentions to liquidate the entity or to cease operations.
- Loss of key management without replacement.
- Loss of a major market, key customer(s), franchise, license, or principal supplier(s).
- Labor difficulties.
- Shortages of important supplies.
- Emergence of a highly successful competitor.

#### Other

- Non-compliance with capital or other statutory or regulatory requirements, such as solvency or liquidity requirements for financial institutions.
- Pending legal or regulatory proceedings against the entity that may, if successful, result in claims that the entity is unlikely to be able to satisfy.



- Changes in law or regulation or government policy expected to adversely affect the entity.
- Uninsured or underinsured catastrophes when they occur.
- Substantial decrease in share price.

The significance<sup>9a</sup> of such events or conditions often can be mitigated by other factors. For example, the effect of an entity being unable to make its normal debt repayments may be counter-balanced by management's plans to maintain adequate cash flows by alternative means, such as by disposing of assets, rescheduling loan repayments, or obtaining additional capital. Similarly, the loss of a principal supplier may be mitigated by the availability of a suitable alternative source of supply.

A3-1. The auditor's identification of events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern in accordance with paragraph 10-1 is before consideration of any related mitigating factors (i.e., management's plans for future actions in relation to events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern).

#### *The Entity and Its Environment*

The Entity's Business Model, Objectives, Strategies and Related Business Risks (Ref: Para. 10-2(a))

A3-2. In accordance with ISA (UK) 315 (Revised June 2016), the auditor is required to obtain an understanding of the entity's objectives, strategies and related business risks that may result in risks of material misstatement. Such an understanding will assist the auditor in obtaining information that is relevant in identifying events or conditions that may cast significant doubt on the entity's ability to continue as a going concern and whether a material uncertainty related to going concern exists. For example:

- Developments in the industry or economic environment where the entity operates (e.g., a potential related business risk might be increased costs, loss of market share)
- New products and services (e.g., a potential related business risk might be that there is increased product liability).
- Expansion of the business (e.g., a potential related business risk might be that the demand has not been accurately estimated).
- Current and prospective financing requirements (e.g., a potential business risk might be current financing requirements approach maturity without realistic

<sup>9a</sup> Significance is defined in the Glossary of Terms as "the relative importance of a matter, taken in context. The significance of a matter is judged by the practitioner in the context in which it is being considered. This might include, for example, the reasonable prospect of its changing or influencing the decisions of intended users of the practitioner's report; or, as another example, where the context is a judgment about whether to report a matter to those charged with governance, whether the matter would be regarded as important by them in relation to their duties. Significance can be considered in the context of quantitative and qualitative factors, such as relative magnitude, the nature and effect on the subject matter and the expressed interests of intended users or recipients".

prospects of renewal or repayment, or reliance on short-term borrowings to finance long-term assets).

Examples of events or conditions, that may cast significant doubt on the entity's ability to continue as a going concern are included in paragraph A3.

A3-3. Some business risks may be so significant that they highlight uncertainties related to events or conditions, that individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.

The nature of the entity, including its operations, the types of investments the entity is making and plans to make, and how the entity is structured and financed (Ref: Para. 10-2(b))

A3-4. An understanding of the nature of the entity enables the auditor to understand such matters as:

- Whether the entity has a complex structure. Larger or more complex entities may give rise to increased susceptibility to events and conditions that may cast significant doubt on the entity's ability to continue as a going concern.
- Whether the entity has any financial obligations, undertakings, and guaranties arranged with other entities such as lenders, suppliers and group entities, and the terms of any borrowing facilities and supplier credit (see also A8-11–A8-14).

The measurement and review of the entity's financial performance, including forecasts, future cash flows, and management's budgeting processes (Ref: Para 10-2(c))

A3-5. When assessing the entity's ability to continue as a going concern, as described in paragraph A3-11, management may use historical information and information available about the future from internally generated sources such as:

- Key performance indicators (financial and non-financial) and key ratios, trends and operating statistics.
- Period-on-period financial performance analyses.
- Budgets, forecasts, variance analyses, segment information and divisional, departmental or other level performance reports.
- Cash flow requirements (in relation to operating activities, investing activities and financing activities).
- Comparisons of an entity's performance with that of competitors.

A3-6. Internal measures may also highlight unexpected results or trends that may indicate the existence of events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. For example, performance measures may indicate an unusual deterioration in sales volume when compared to that of other entities in the same industry.

A3-7. Management may also use information from external sources in management's measurement process, such as pricing related data, macro-economic data (e.g., economic growth rates), credit history data or industry specific data. Externally generated data might be used to, for example, assess whether there are any economic, political or other factors which may cause the market to change, or assess whether the entity's products or services are compatible with market projections in terms of market position, quality and expected life.

A3-8. Depending on the size, complexity, and particular circumstances of the entity, including the entity's business risks, management might prepare forecasts and future cash flows, or other equivalent analysis, for the purposes of assessing going concern (see also A3-11).

*The Requirements of the Applicable Financial Reporting Framework* (Ref: Para. 10-2(d))

A3-9. Obtaining an understanding of the requirements of the applicable financial reporting framework provides the auditor with a basis for discussion with management, and, where applicable, those charged with governance about how management has applied the requirements relevant to going concern, and about the auditor's determination of whether they have been applied appropriately. The auditor may also consider guidance issued by regulatory, enforcement or supervisory authorities in respect of going concern matters.<sup>9b</sup>

*The Entity's Internal Control*

*The Nature and Extent of Oversight and Governance* (Ref: Para. 10-2(e))

A3-10. The governance and management functions, attitudes, awareness, and actions of management and those charged with governance form part of the entity's control environment. The control environment sets the tone of an organization, influencing the control consciousness of its people, and is influenced significantly by those charged with governance, because one of their roles is to counterbalance pressures on management in relation to financial reporting. Accordingly, the effectiveness of management's assessment of the entity's ability to continue as a going concern may be influenced by the oversight and governance that the entity has in place over management's process for making the assessment of the entity's ability to continue as a going concern.

A3-11. The auditor may obtain an understanding of whether those charged with governance:

- Have the skills or knowledge to understand the characteristics of a method used by management in assessing the entity's ability to continue as a going concern;
- Have the skills and knowledge to understand whether management's assessment has been made in accordance with the requirements of the applicable financial reporting framework;
- Have the information required to evaluate how management made the assessment, and the authority to call into question management's actions when those actions appear to be inadequate or inappropriate; or
- Oversee management's process for making the assessment.

<sup>9b</sup> For example, the IFRS Interpretations Committee issued Agenda Decision *Disclosure requirements relating to assessment of going concern (IAS 1)* in July 2014. The FRC issued *Guidance on the Going Concern Basis of Accounting and Reporting on Solvency and Liquidity Risks* (April 2016) and for entities that apply the UK Corporate Governance Code: *Guidance on Risk Management, Internal Control and Related Financial and Business Reporting* (September 2014) and *Guidance for Directors of Banks on Solvency and Liquidity Risk Management and the Going Concern Basis of Accounting* (September 2014).

A3-12. Obtaining an understanding of the oversight by those charged with governance may be particularly important when the assessment of the entity's ability to continue as a going concern:

- Requires significant judgment by management to address material uncertainties; or
- Is complex to make, for example, because of the use of multiple data sources or assumptions with complex interrelationships.

Management's Identification of the Relevant Methods, Assumptions and Sources of Data  
(Ref: Para. 10-1(h)(ii))

A3-13. Management identifies the method that is appropriate in assessing the entity's ability to continue as a going concern. In some instances, the method used by management may be a complex method that requires input from multiple sources of historical and forward-looking data or assumptions, with multiple interrelationships between them. In other cases, management may determine that the most appropriate method is to prepare cash flow forecasts and budgets or other equivalent analysis covering the appropriate assessment period.

A3-14. In obtaining an understanding of how management identifies the relevant method, assumptions and data that are appropriate in assessing the entity's ability to continue as a going concern, the auditor understands the basis for management's selection of the method, data and assumptions, including, for example:

- How management determines the relevance and accuracy of the method.
- How management determines that the assumptions are relevant and complete.
- The nature and source of the method, data and assumptions, including information obtained from an external information source.
- If alternative methods, assumptions or data were considered by management.
- Where relevant, the requirements of the applicable financial reporting framework.
- The period of time used by management to make its assessment.

A3-15. A review of the outcome of previous forecasts (retrospective review) may also assist the auditor in obtaining information regarding the effectiveness of management's process for assessing going concern.

#### *Risk Assessment Procedures*

A3-16. ISA (UK) 315 (Revised June 2016) requires the auditor to obtain an understanding of certain matters about the entity and its environment, the applicable financial reporting framework and the entity's internal control. The requirements in paragraph 10-1–10-2 of this ISA (UK) relate more specifically to going concern and are supplemental to the broader requirements in ISA (UK) 315 (Revised June 2016).

A3-17. Risk assessment procedures that are relevant to the requirement in paragraphs 10-1–10-2 may include the following:

- Analyzing and discussing the entity's latest available interim financial statements and management accounts.

- Reading the terms of debentures and loan agreements and determining whether any have been breached.
- Reading minutes of the meetings of shareholders, those charged with governance and relevant committees for reference to financing difficulties.
- Reading minutes of meetings of management, and, where applicable, those charged with governance and correspondence between the entity and providers of finance.
- Inquiring of the entity's legal counsel regarding the existence of litigation and claims and the reasonableness of management's assessments of their outcome and the estimate of their financial implications.

A4. The risk assessment procedures required by paragraph 10-1-10-2 help the auditor to determine whether management's use of the going concern basis of accounting is likely to be an important issue and its impact on planning the audit. These procedures also allow for more timely discussions with management, including a discussion of management's plans and resolution of any identified going concern issues.

A4-1. The nature, timing and extent of the auditor's risk assessment procedures to obtain the understanding required in paragraphs 10-1-10-2 may depend on the extent to which the individual matter(s) apply in the circumstances. For example, some smaller entities may not have an independent governance structure, and the role of governance may be undertaken directly by the owner-manager. Accordingly, some considerations about the nature and extent of oversight and governance the entity has in place may be less relevant or not applicable. Furthermore, management's method to assess the entity's ability to continue as a going concern may be uncomplicated because the business activities are simple, or the business is affected to a lesser degree by events and conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern. In such circumstances, the auditor's risk assessment procedures are likely to be less extensive.

A4-2. In contrast, in a larger entity with a complex structure and complex borrowing arrangements, management's method to assess the entity's ability to continue as a going concern may be complex and require significant judgments by management. In addition, the entity may have more extensive controls over management's method. If so, the nature or timing of the auditor's risk assessment procedures are likely to be different, or more extensive, than in the circumstances described in paragraph A4-1.

*Considerations Specific to Smaller Entities* (Ref: Para. 10-1-10-3)

A5. The following considerations may be relevant for entities with only simple businesses, which may include many smaller entities:

- The size of an entity may affect its ability to withstand adverse conditions. Small entities may be able to respond quickly to exploit opportunities but may lack reserves to sustain operations.
- Conditions of particular relevance to small entities include the risk that banks and other lenders may cease to support the entity, as well as the possible loss of a principal supplier, major customer, key employee, or the right to operate under a license, franchise or other legal agreement.

*Period beyond Management's Assessment* (Ref: Para. 10-4)

- A6-1. As required by paragraph 11, the auditor remains alert to the possibility that there may be known events, scheduled or otherwise, or conditions that will occur beyond the period of assessment used by management that may bring into question the appropriateness of management's use of the going concern basis of accounting in preparing the financial statements. Since the degree of uncertainty associated with the outcome of an event or condition increases as the event or condition is further into the future, in considering events or conditions further in the future, the indications of going concern issues need to be significant before the auditor needs to consider taking further action. If such events or conditions are identified, the auditor may need to request management to evaluate the potential significance of the event or condition on its assessment of the entity's ability to continue as a going concern. In these circumstances the procedures in paragraphs 12-1–12-2 apply.
- A6-2. Other than inquiry of management, the auditor does not have a responsibility to perform any other audit procedures to identify events or conditions that may cast significant doubt on the entity's ability to continue as a going concern beyond the period assessed by management, which, as discussed in paragraph 13, would be at least twelve months from the date of the financial statements.

*Remaining Alert throughout the Audit for Audit Evidence about Events or Conditions*

(Ref: Para. 11)

- A6-3. Audit evidence is cumulative in nature and is primarily obtained from audit procedures performed during the course of planning and performing the audit. The process of identifying events or conditions, which may cast significant doubt on the entity's ability to continue as a going concern continues as the audit progresses. For example, ISA (UK) 315 (Revised June 2016) requires the auditor to identify and assess the risks of material misstatement at the financial statement level and at the assertion level for classes of transactions, account balances, and disclosures. The identification and assessment of risk of material misstatement may provide the auditor with audit evidence of events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. For example, a risk of material misstatement associated with the valuation assertion for a lender of medium-term real estate backed loans has been identified because of a fall in real estate market values. The same event in combination with a severe economic downturn may have a longer-term consequence, and a greater impact on the assessment of the risk of material misstatement that may indicate an event or condition that may cast significant doubt on the entity's ability to continue as a going concern.
- A7. Correspondingly, ISA (UK) 315 (Revised June 2016) requires the auditor to revise the auditor's risk assessment and modify the further planned audit procedures accordingly when additional audit evidence is obtained during the course of the audit that affects the auditor's assessment of risk.<sup>10</sup> If events or conditions that may cast significant doubt on the entity's ability to continue as a going concern are identified after the auditor's risk assessments are made, in addition to performing the procedures in paragraph 16, the auditor's assessment of the risks of material misstatement may need to be revised. The

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<sup>10</sup> ISA (UK) 315 (Revised June 2016), paragraph 31.

existence of such events or conditions may also affect the nature, timing and extent of the auditor's further procedures in response to the assessed risks. ISA (UK) 330 (Revised July 2017)<sup>11</sup> establishes requirements and provides guidance on this issue.

A7-1. The auditor may also become aware of events or conditions through:

- The auditor's preliminary engagement and planning activities in accordance with ISA (UK) 300 (Revised June 2016).<sup>11a</sup>
- The auditor's consideration of the other information in accordance with ISA (UK) 720 (Revised June 2016).<sup>11b</sup>
- Other engagements performed for the entity (e.g., an agreed-upon procedures engagement relating to an entity's debt covenant compliance).
- Other external market information (e.g., risk factors such as profit warnings or short-selling of shares; forward-looking information such as economic or earnings forecasts).

*Identification of Previously Unidentified or Undisclosed Events or Conditions (Ref: Para. 11-1)*

A7-2. Where the auditor identifies events or conditions that may cast significant doubt on the entity's ability to continue as a going concern that management failed to identify or disclose, the auditor determines whether there is a significant deficiency in internal control with regard to the entity's risk assessment processes in accordance with ISA (UK) 265.<sup>11c</sup>

A7-3. The requirements and guidance in ISA (UK) 240 (Revised June 2016) regarding the auditor's responsibilities relating to fraud in an audit of financial statements are relevant where management appears to have intentionally failed to disclose a material uncertainty related to going concern to the auditor. The auditor may also consider whether it is necessary to re-evaluate the reliability of management's responses to the auditor's inquiries and management's representations to the auditor.

## **Evaluating Management's Assessment**

*Management's Method and Supporting Analysis and the Auditor's Evaluation (Ref: Para. 12-2)*

A8. Evaluating management's method to assess the entity's ability to continue as a going concern is a key part of the auditor's consideration of management's use of the going concern basis of accounting.

A8-1. Audit procedures that are also relevant to the requirement in paragraphs 12-1–12-2 may include the following:

- Confirming the existence, legality and enforceability of arrangements to provide or maintain financial support with related and third parties and assessing the

<sup>11</sup> ISA (UK) 330 (Revised July 2017), *The Auditor's Responses to Assessed Risks*.

<sup>11a</sup> ISA (UK) 300 (Revised June 2016), *Planning an Audit of Financial Statements*.

<sup>11b</sup> ISA (UK) 720 (Revised June 2016), *The Auditor's Responsibilities Relating to Other Information*.

<sup>11c</sup> ISA (UK) 265, *Communicating Deficiencies in Internal Control to Those Charged With Governance and Management*, paragraph 8.

financial ability of such parties to provide additional funds (see also paragraphs A8-10–A8-12).

- Evaluating the entity's plans to deal with unfilled customer orders.
- Performing audit procedures regarding subsequent events to identify those that either mitigate or otherwise affect the entity's ability to continue as a going concern.
- Confirming the existence, terms and adequacy of borrowing facilities (see also paragraphs A8-13–A8-14).
- Obtaining and reviewing reports of regulatory actions.
- Determining the adequacy of support for any planned disposals of assets.

A8-2. In addition to the procedures required in paragraph 12-2, the auditor may compare:

- The prospective financial information for recent prior periods with historical results; and
- The prospective financial information for the current period with results achieved to date.

Performing audit procedures helps the auditor obtain information regarding the effectiveness of management's method for making its assessment and determine the susceptibility of management's method to possible management bias. The auditor's professional skepticism also assists in identifying such circumstances or conditions and in determining the nature, timing and extent of further audit procedures.

Method (Ref: Para. 12-2(a))

A8-3. Matters that may be relevant to the auditor's consideration of whether the method selected is appropriate in the context of the applicable financial reporting framework include whether the method used is consistent with methods used in other areas of the entity's business activities. For example, management's selection and application of methods used in making accounting estimates (see also paragraph A8-7).

Relevance and Reliability of Data (Ref: Para. 12-2(b))

A8-4. Matters the auditor may consider when evaluating the relevance and reliability of the underlying data used to make the assessment, may include, for example: the appropriateness of management's rationale for the selection of the data, the source of the data, or the consistency of the data used with data used in previous periods.

A8-5. ISA (UK) 500 requires the auditor to evaluate whether the information is sufficiently reliable for the auditor's purposes, including as necessary in the circumstances, to obtain audit evidence about the accuracy and completeness of the information and evaluate whether the information is sufficiently precise and detailed for the auditor's purposes.<sup>11d</sup>

Assumptions (Ref: Para. 12-2(c))

A8-6. Matters the auditor may consider when determining if there is adequate support for the assumptions used by management include, for example:

<sup>11d</sup> ISA (UK) 500, *Audit Evidence*, paragraph 9.



- Management's rationale for the selection of the assumptions.
- Whether a change from prior periods in selecting an assumption is based on new circumstances or new information. When it is not, the change may not be reasonable or may be an indicator of possible management bias.
- Whether and, if so, how management considered alternative assumptions by, for example, performing a sensitivity analysis, including 'pessimistic' and 'optimistic' scenarios, to determine the effect of changes in the assumptions on the data used in making the assessment.

A8-7. Matters that may be relevant to the auditor's consideration of whether the assumptions selected are appropriate in the context of the applicable financial reporting framework include whether the assumptions used are consistent with those used in other areas of the entity's business activities. Such matters may include, for example, business prospects, assumptions in strategy documents and assumptions used in the making of accounting estimates (e.g., impairment of goodwill, deferred tax assets).

A8-8. Management's rationale for the selection of assumptions may be based on management's intent and ability to carry out specific courses of action.

*Evaluating Management's Plans for Future Actions* (Ref: Para. 12-2(d))

A8-9. The significance of events and conditions may be mitigated by management's plans for future actions. Management may document plans for future actions that are relevant to specific assets or liabilities, including, for example, its plans to liquidate assets, borrow money or restructure debt, reduce or delay expenditures, or increase capital. Such plans are relevant to the auditor's evaluation of the appropriateness of management's use of the going concern basis of accounting, including management's intent and ability to carry out such plans. The nature and extent of audit evidence to be obtained about management's intent and ability is a matter of professional judgment. When applicable, the auditor's procedures may include the following:

- Inquiry of management about its reasons for a particular course of action.
- Review of management's history of carrying out its stated intentions.
- Inspection of written plans and other documentation, including, when applicable, formally approved budgets, authorizations or minutes.
- Review of events occurring subsequent to the date of the financial statements and up to the date of the auditor's report.
- Evaluation of the entity's ability to carry out a particular course of action given the entity's economic circumstances, including the implications of its existing commitments and legal, regulatory, or contractual restrictions that could affect the feasibility of management's actions.

A8-10. Where management's plans for future actions are based on continued support by third parties, whether through the subordination of loans, commitments to maintain or provide additional funding, or guarantees, and such support is important to an entity's ability to continue as a going concern, the auditor may need to consider requesting an external confirmation<sup>11e</sup> (including of terms and conditions) from those third parties and

<sup>11e</sup> ISA (UK) 330 (Revised June 2016), paragraph 19.

to obtain evidence of their ability to provide such support (see also paragraphs A8-13–A8-15).

A8-11. The auditor also considers the business rationale for continued support, particularly if the entity is loss making, including what that support is predicated on (e.g., business or transformation plan, forecasts).

#### *Considerations for smaller entities*

A8-12. Continued support by owner-managers is often important to smaller entities' ability to continue as a going concern. Where a small entity is largely financed by a loan from the owner-manager, it may be important that these funds are not withdrawn. For example, the continuance of a small entity in financial difficulty may be dependent on the owner-manager subordinating a loan to the entity in favor of banks or other creditors, or the owner-manager supporting a loan for the entity by providing a guarantee with his or her personal assets as collateral. In such circumstances, the auditor may obtain appropriate documentary evidence of the subordination of the owner-manager's loan or of the guarantee. Where an entity is dependent on additional support from the owner-manager, the auditor may evaluate the owner-manager's ability to meet the obligation under the support arrangement. In addition, the auditor may request written confirmation of the terms and conditions attaching to such support and the owner-manager's intention or understanding.

#### The Auditor's Examination of Borrowing Facilities

A8-13. As described in A-10, in certain circumstances, the auditor may decide that it is necessary to obtain confirmations of the existence and terms of borrowing facilities and make an assessment of the intentions of those providing the facilities when, for example:

- Headroom between the financial resources required and available to the entity is marginal.
- The entity is dependent on borrowing facilities shortly due for renewal.
- Correspondence between the lender and the entity indicates that the last renewal of facilities was agreed with difficulty, or that, since the last review of facilities, the lender has imposed additional conditions as a prerequisite for continued lending.
- A significant deterioration in cash flow is projected.
- The value of assets granted as security for the borrowings is declining.
- The entity has breached the terms of borrowing covenants, or there are indications of potential breaches.

A8-14. Some finance providers may be reluctant to confirm to an entity or their auditor that borrowing facilities will be renewed. This situation may extend to entities with a profitable business and relatively small borrowing requirements. The lack of a positive confirmation from a finance provider does not in and of itself provide evidence of a material uncertainty related to going concern. However, if the auditor concludes that confirmation of the facilities are being refused for reasons that are specific to the entity's circumstances, the auditor considers the significance of this and, where appropriate, discusses with management whether there are alternative strategies or

sources of financing that may mitigate events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern.

*Written Representations* (Ref: Para. 12-2(f))

A8-15. The auditor may consider it appropriate to obtain specific written representations beyond those required in paragraph 12(f) in support of audit evidence obtained regarding management's plans for future actions in relation to its going concern assessment and the feasibility of those plans. However, such representations do not provide sufficient appropriate audit evidence on their own about any of the matters with which they deal.<sup>11f</sup>

A9. It is not the auditor's responsibility to rectify the lack of analysis by management. In some circumstances, however, the lack of detailed analysis by management to support its assessment may not prevent the auditor from concluding whether management's use of the going concern basis of accounting is appropriate in the circumstances. For example, when there is a history of profitable operations and a ready access to financial resources, management may make its assessment without detailed analysis. In this case, the auditor's evaluation of the appropriateness of management's assessment may be made without performing detailed evaluation procedures if the auditor's other audit procedures are sufficient to enable the auditor to conclude whether management's use of the going concern basis of accounting in the preparation of the financial statements is appropriate in the circumstances.

*Professional Skepticism* (Ref: Para. 12D-3)

A10-1. The auditor is required by ISA (UK) 200 (Revised June 2016) to plan and perform the audit with professional skepticism. Maintaining professional skepticism requires an ongoing questioning of whether the information and audit evidence obtained suggests that a material uncertainty related to going concern exists.

*The Period of Management's Assessment* (Ref: Para. 13-1)

A11. Most financial reporting frameworks requiring an explicit management assessment specify the period for which management is required to take into account all available information.<sup>12</sup>

<sup>11f</sup> ISA (UK) 580, *Written Representations*, paragraph 4.

<sup>12</sup> Accounting frameworks do not normally specify a maximum period that should be reviewed as part of the assessment of going concern. However, IAS 1 and FRS 102 both require that management takes into account all available information about the future.

For example, IAS 1 defines this as a period that should be at least, but is not limited to, twelve months from the end of the reporting period.

FRS 102 requires that in assessing whether the going concern basis of accounting is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the date when the financial statements are authorized for issue.

## Relevant Information (Ref: Para. 13-1)

- A11-1. In the UK, applicable financial reporting frameworks generally specify that management takes into account all available information about the future.<sup>12a</sup> In evaluating management's assessment of the entity's ability to continue as a going concern, the auditor may inquire of management and those charged with governance as to what information is available about the future and determine whether this has been appropriately considered as part of management's assessment. For example, relevant information may be available to management through business planning activities, risk management processes, regulatory reporting, planning or communications with regulatory, enforcement or supervisory authorities.
- A11-2. For entities that are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, or to explain why they have not, information that has been developed to support reporting about the entity's business model, principal risks and the entity's longer-term viability statement will also be relevant to management's assessment of the entity's ability to continue as a going concern.
- A11-3. When evaluating management's assessment in accordance with paragraph 13-1, relevant information of which the auditor is aware will include information derived from audit procedures carried out during the audit engagement, and from other sources such as information obtained from the auditor's previous experience with the entity or the firm's quality control procedures (e.g., acceptance and continuance of client relationships and specific engagements).

*Considerations Specific to Smaller Entities* (Ref: Para. 12-1–13-1)

- A11-4. A determination of the sufficiency and appropriateness of evidence supplied to the auditor by those charged with governance will depend on the particular circumstances. For example, to be sufficient the evidence may not require formal cash flow forecasts and budgets to have been prepared for the period ending one year from the date of approval of the financial statements. Although such forecasts and budgets are likely to provide the most persuasive evidence, alternative sources of evidence may also be acceptable. This is particularly likely to be the case in respect of entities with uncomplicated circumstances. Many smaller companies fall into this category.
- A12. In many cases, the management of smaller entities may not have a detailed method to assess the entity's ability to continue as a going concern, but instead may rely on in-depth knowledge of the business and anticipated future prospects. Nevertheless, in accordance with the requirements of this ISA (UK), the auditor needs to evaluate management's method to assess the entity's ability to continue as a going concern. For smaller entities, it may be appropriate to discuss the medium and long-term financing of the entity with management, provided that management's contentions can be corroborated by sufficient documentary evidence and are not inconsistent with the auditor's understanding of the entity. Therefore, the requirement in paragraph 14-1 for the auditor to request management to extend its assessment may, for example, be satisfied by discussion, inquiry and inspection of supporting documentation, for

<sup>12a</sup> For example, IAS 1, paragraph 26 and FRS 102, *The Financial Reporting Standard applicable in the UK and Republic of Ireland*, paragraph 3.8 both require that management takes into account all available information about the future.

example, orders received for future supply, evaluated as to their feasibility or otherwise substantiated.

**Management Unwilling to Make or Extend Its Assessment (Ref: Para. 15-1)**

A13-1. In certain circumstances, the auditor may believe it necessary to request management to make or extend its assessment. If management is unwilling to do so, the auditor may discuss the matter with management or, as appropriate those charged with governance, as they may be able to provide additional audit evidence to support their assertion that the use of the going concern basis of accounting is appropriate.

**UK Corporate Governance Code Reporting – Statement on the Directors' Assessment of the Ongoing Viability of the Entity (Ref: Para. 16-1)**

A16-1. Determining the nature and extent of procedures to address the requirements in paragraph 16-1 is a matter of professional judgment. Examples of such procedures include:

- Obtaining an understanding of the management's method to assess the entity's viability.
- Obtaining and considering management's assessment of the entity's viability and the underlying supporting documents.
- Considering the appropriateness of the assessment period used by management over which viability is assessed (see also paragraph A16-2).
- Where management has prepared cash flow forecasts:
  - Checking whether the calculations within the cash flow forecasts are arithmetically accurate.
  - Considering whether there are inconsistencies between the cash flow forecasts prepared to support the viability assessment and those prepared for other purposes (e.g., for going concern, impairment, deferred taxation). In most cases, the auditor would expect the underlying data generated to prepare the forecasts to be the same, whilst recognizing there may be permissible differences between certain items in the individual forecasts (e.g., remedial actions).
- Where management have considered a range of alternative outcomes by, for example, performing a sensitivity analysis to determine the effect of changes in the significant assumptions or the data used in assessing the entity's viability, considering the appropriateness of the outcomes.
- Considering whether the statements and disclosures made in the annual report as described in paragraph 16-1 comply with the relevant provisions of the UK Corporate Governance Code and are consistent with:
  - Management's assessment of the entity's viability and the underlying supporting documents.
  - Management's assessment of the entity's ability to continue as a going concern, including all relevant information of which the auditor is aware as a result of the audit.

A16-2. Management may use the same period of assessment for the ongoing viability of the entity as they use for the assessment of the entity's ability to continue as a going concern or they may use different periods of assessment. Where the period applied by management is different, the auditor considers whether this is appropriate given the nature and circumstances of the entity, including its size and complexity. The length of the period is also likely to depend upon such factors as:

- The entity's reporting and budgeting systems.
- Investment and planning time horizons.

### **Evaluating the Sufficiency and Appropriateness of Audit Evidence Obtained**

(Ref: Para. 17-1)

A17-1. Paragraph 9-1(b) explains that a material uncertainty related to going concern exists when the magnitude of the potential impact of the events or conditions and the likelihood of occurrence is such that appropriate disclosure is necessary to achieve fair presentation (for fair presentation frameworks) or for the financial statements not to be misleading (for compliance frameworks). The auditor is required by paragraph 17-1(a) to conclude whether such a material uncertainty related to going concern exists regardless of whether or how the applicable financial reporting framework defines a material uncertainty.

Management Unwilling to Make or Extend Its Assessment (Ref: Para. 17-2)

A18-1. If management or, as appropriate, those charged with governance, do not provide sufficient information, the auditor considers the impact on the auditor's report:

- Where the financial reporting framework requires management to make a specific assessment of the entity's ability to continue as a going concern, or where the financial reporting framework specifies the period that should be reviewed as part of that assessment, a qualified opinion or an adverse opinion in the auditor's report may be appropriate, because the financial statements have not been prepared, in all material respects, in accordance with the requirements of the applicable financial reporting framework.
- Where the financial reporting framework does not require management to make a specific assessment of the entity's ability to continue as a going concern, a qualified opinion or a disclaimer of opinion in the auditor's report may be appropriate, because it may not be possible for the auditor to obtain sufficient appropriate audit evidence regarding management's use of the going concern basis of accounting in the preparation of the financial statements, such as audit evidence regarding the existence of plans management has put in place or the existence of other mitigating factors.

Management Bias (Ref: Para. 18-1(a))

A19-1. When the auditor identifies indicators of possible management bias, the auditor may need a further discussion with management and may need to reconsider whether sufficient appropriate audit evidence has been obtained. An example of an indicator of possible management bias with respect to management's assessment of the entity's ability to continue as a going concern may be where management has made assumptions or selected data that only yield a favorable outcome.

A19-2. Indicators of possible management bias may affect the auditor's conclusions in respect of management's assessment of the entity's ability to continue as a going concern. Such indicators may have wider implications for other aspects of the audit such as whether the auditor's risk assessment and related responses remain appropriate. Where there is intention to mislead, management bias is fraudulent in nature.

A19-3. The auditor may also need to consider the implications for other aspects of the audit, for example, the need to further question the appropriateness of management's judgments in making accounting estimates. Further, indicators of possible management bias may affect the auditor's conclusion as to whether the financial statements as a whole are free from material misstatement, as discussed in ISA (UK) 700 (Revised June 2016). In accordance with ISA (UK) 705 (Revised June 2016), where the auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor expresses a qualified opinion or disclaims an opinion.

### **Disclosures Related to Going Concern**

#### *Appropriateness of Disclosures when Events or Conditions Have Been Identified and a Material Uncertainty Related to Going Concern Exists* (Ref: Para. 19)

A23. Paragraph 19 requires the auditor to determine whether the financial statement disclosures address the matters set forth in that paragraph. This determination is in addition to the auditor determining whether disclosures about a material uncertainty, required by the applicable financial reporting framework, are adequate. Disclosures required by some financial reporting frameworks that are in addition to matters set forth in paragraph 19 may include disclosures about:

- Management's evaluation of the significance of the events or conditions relating to the entity's ability to meet its obligations; or
- Significant judgments made by management as part of its assessment of the entity's ability to continue as a going concern.

Some financial reporting frameworks may provide additional guidance regarding management's consideration of disclosures about the magnitude of the potential impact of the principal events or conditions, and the likelihood and timing of their occurrence.

#### *Appropriateness of Disclosures When Events or Conditions Have Been Identified but No Material Uncertainty Related to Going Concern Exists* (Ref: Para. 20)

A24. Even when no material uncertainty related to going concern exists, paragraph 20 requires the auditor to evaluate whether, in view of the requirements of the applicable financial reporting framework, the financial statements provide appropriate disclosure about events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. Some financial reporting frameworks may address disclosures about:

- Principal events or conditions;
- Management's evaluation of the significance of those events or conditions in relation to the entity's ability to meet its obligations;
- Management's plans that mitigate the effect of these events or conditions; or

- Significant judgments made by management as part of its assessment of the entity's ability to continue as a going concern.

A25. When the financial statements are prepared in accordance with a fair presentation framework, the auditor's evaluation as to whether the financial statements achieve fair presentation includes the consideration of the overall presentation, structure and content of the financial statements, and whether the financial statements, including the related notes, represent the underlying transactions and events in a manner that achieves fair presentation.<sup>13</sup> Depending on the facts and circumstances, the auditor may determine that additional disclosures are necessary to achieve fair presentation. This may be the case, for example, when events or conditions have been identified that may cast significant doubt on the entity's ability to continue as a going concern but, based on the audit evidence obtained, the auditor concludes that no material uncertainty related to going concern exists, and no disclosures are explicitly required by the applicable financial reporting framework regarding these circumstances.

#### Implications for the Auditor's Report

##### *Use of Going Concern Basis of Accounting is Inappropriate* (Ref: Para. 21)

A26. If the financial statements have been prepared using the going concern basis of accounting but, in the auditor's judgment, management's use of the going concern basis of accounting in the financial statements is inappropriate, the requirement in paragraph 21 for the auditor to express an adverse opinion applies regardless of whether or not the financial statements include disclosure of the inappropriateness of management's use of the going concern basis of accounting.

A27. When the use of the going concern basis of accounting is not appropriate in the circumstances, management may be required, or may elect, to prepare the financial statements on another basis (e.g., liquidation basis). The auditor may be able to perform an audit of those financial statements provided that the auditor determines that the other basis of accounting is acceptable in the circumstances. The auditor may be able to express an unmodified opinion on those financial statements, provided there is appropriate disclosure therein about the basis of accounting on which the financial statements are prepared, but may consider it appropriate or necessary to include an Emphasis of Matter paragraph in accordance with ISA (UK) 706 (Revised June 2016)<sup>14</sup> in the auditor's report to draw the user's attention to that alternative basis and the reasons for its use.

##### *Use of Going Concern Basis of Accounting is Appropriate* (Ref: Para. 21-1)

A27-1. The amount of detail to be provided in the auditor's report to explain how the auditor evaluated management's assessment of the entity's ability to continue as a going concern is a matter of professional judgment. In accordance with paragraph 21-1, the auditor may describe:

- Aspects of the auditor's response or approach that were most relevant to the evaluation of management's assessment.

<sup>13</sup> ISA (UK) 700 (Revised June 2016), *Forming an Opinion and Reporting on Financial Statements*, paragraph 14.

<sup>14</sup> ISA (UK) 706 (Revised June 2016), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*.



- A brief overview of the procedures performed by the auditor.
- An indication of the outcome of the auditor's procedures.

A27-2. Paragraph 39(b)(iv) of ISA (UK) 700 (Revised June 2016) requires the auditor to describe in the auditor's report the auditor's responsibilities relating to management's use of the going concern basis of accounting and the disclosure of material uncertainties. When describing these responsibilities, the auditor may choose to include this description either:

- (a) in the Conclusions Relating to Going Concern section of the auditor's report; or
- (b) in the Auditor's Responsibilities for the Audit of the Financial Statements section of the auditor's report,

and cross-refer from the respective section as appropriate.

A27-3. Auditor's reports which include a description of the auditor's responsibilities relating to management's use of the going concern basis of accounting and the disclosure of material uncertainties in the Conclusions Relating to Going Concern section of the auditor's report will include the minimum elements of an auditor's report required by paragraph 50(k) of ISA 700 (Revised) and therefore the auditor is not precluded from being able to assert compliance with International Standards on Auditing issued by the IAASB.

*Use of Going Concern Basis of Accounting Is Appropriate but a Material Uncertainty Related to Going Concern Exists* (Ref: Para. 22–23)

A28. The identification of a material uncertainty related to going concern is a matter that is important to users' understanding of the financial statements. The use of a separate section with a heading that includes reference to the fact that a material uncertainty related to going concern exists alerts users to this circumstance.

A29. The Appendix<sup>14a</sup> to this ISA (UK) provides illustrations of the statements that are required to be included in the auditor's report on the financial statements when International Financial Reporting Standards (IFRSs) is the applicable financial reporting framework. If an applicable financial reporting framework other than IFRSs is used, the illustrative statements presented in the Appendix to this ISA may need to be adapted to reflect the application of the other financial reporting framework in the circumstances.

A30. Paragraph 22 establishes the minimum information required to be presented in the auditor's report in each of the circumstances described. The auditor may provide additional information to supplement the required statements, for example to explain:

- That the existence of a material uncertainty related to going concern is fundamental to users' understanding of the financial statements;<sup>15</sup> or
- How the matter was addressed in the audit. (Ref: Para. A1)

<sup>14a</sup> The examples in the Appendix have not been tailored for the UK. Illustrative auditor's reports tailored for use with audits conducted in accordance with ISAs (UK) are given in the current version of the FRC's Compendium of Illustrative Auditor's Reports.

<sup>15</sup> ISA (UK) 706 (Revised June 2016), paragraph A2.

A30-1. In the UK, the requirement in legislation<sup>15a</sup> to include a statement on any material uncertainty relating to going concern is met by the requirements of paragraph 22.

**Appropriate Disclosure of a Material Uncertainty Related to Going Concern Is Made in the Financial Statements (Ref: Para. 22)**

A31. Illustration 1 of the Appendix<sup>15b</sup> to this ISA (UK) is an example of an auditor's report when the auditor has obtained sufficient appropriate audit evidence regarding the appropriateness of management's use of the going concern basis of accounting but a material uncertainty related to going concern exists and appropriate disclosure is made in the financial statements. The Appendix of ISA (UK) 700 (Revised June 2016) also includes illustrative wording to be included in the auditor's report for all entities in relation to going concern to describe the respective responsibilities of those responsible for the financial statements and the auditor in relation to going concern.

**Appropriate Disclosure of a Material Uncertainty Related to Going Concern Is Not Made in the Financial Statements (Ref: Para. 23)**

A32. Illustrations 2 and 3 of the Appendix<sup>15b</sup> to this ISA (UK) are examples of auditor's reports containing qualified and adverse opinions, respectively, when the auditor has obtained sufficient appropriate audit evidence regarding the appropriateness of the management's use of the going concern basis of accounting but appropriate disclosure of a material uncertainty related to going concern is not made in the financial statements.

A33. In situations involving multiple uncertainties that are significant to the financial statements as a whole, the auditor may consider it appropriate in extremely rare cases to express a disclaimer of opinion instead of including the statements required by paragraph 22. ISA (UK) 705 (Revised June 2016) provides guidance on this issue.<sup>16</sup>

**Communication with Those Charged with Governance (Ref: Para. 25)**

A34-1. For audits of financial statements of public interest entities, ISA (UK) 260 (Revised June 2016)<sup>16a</sup> requires the auditor to:

- explain the judgments about events or conditions identified in the course of the audit that may cast significant doubt on the entity's ability to continue as a going concern and whether they constitute a material uncertainty related to going concern; and
- provide a summary of all guarantees, comfort letters, undertakings of public intervention and other support measures that have been taken into account when making a going concern assessment,

in the additional report to the audit committee.

<sup>15a</sup> In the UK, Section 495(4) establishes this requirement.

<sup>15b</sup> The examples in the Appendix have not been tailored for the UK. Illustrative auditor's reports tailored for use with audits conducted in accordance with ISAs (UK) are given in the current version of the FRC's Compendium of Illustrative Auditor's Reports.

<sup>16</sup> ISA (UK) 705 (Revised June 2016), paragraph 10.

<sup>16a</sup> ISA (UK) 260 (Revised June 2016), paragraph 16R-2(i).

**Communication with Regulators** (Ref: Para. 25-1)

A35-1. When the auditor of a regulated entity considers that it may be necessary to include a "Material Uncertainty Related to Going Concern" paragraph in the auditor's report or issue a qualified, adverse or disclaimer of opinion in respect of matters related to going concern, the auditor may have a duty to communicate with the applicable regulatory, enforcement or supervisory authorities.

In the UK, in such cases the regulatory, enforcement or supervisory authority might, if it has not already done so, specify corrective action to be taken by the entity.

A35-2. At the time at which the auditor formulates the auditor's report, the auditor takes account of matters such as:

- Any views expressed by the regulatory, enforcement or supervisory authority.
- Any legal advice obtained by those charged with governance.
- The actual and planned corrective action.

A35-3. For audits of public interest entities, ISA (UK) 250 Section B (Revised June 2016)<sup>16b</sup> requires the auditor to report to the relevant regulatory, enforcement or supervisory authority any information about the public interest entity (or an undertaking having close links with the public interest entity) that may bring about a material threat or doubt concerning the continuous functioning of the entity.

A35-4. Where the auditor considers that it may be necessary to include a "Material Uncertainty Related to Going Concern" paragraph in the auditor's report or issue a qualified, adverse or disclaimer of opinion in respect of matters related to going concern and which does not give rise to a responsibility under law, regulation or relevant ethical requirements to report to an appropriate authority outside the entity, the auditor considers whether the matter may be one that ought to be reported in the public interest to an appropriate authority outside the entity and, where this is the case discusses the matter with those charged with governance.<sup>16c</sup>

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<sup>16b</sup> ISA (UK) 250 (Revised June 2016), *Section B—The Auditor's Statutory Right and Duty to Report to Regulators of Public Interest Entities and Regulators of Other Entities in the Financial Sector*, paragraph 13R-1(a)(ii).

<sup>16c</sup> Further guidance on reporting in the public interest is included in ISA (UK) 250 (Revised December 2017), *Section A—Consideration of Laws and Regulations in an Audit of Financial Statements*, paragraphs A33-1–A33-8.